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CLIENT'S tax & financial UPDATE

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A tax, business, and financial planning newsletter for our clients and friends

Year-End Tax Strategies That Might Surprise You

Most taxpayers think that the best way to minimize income tax is by deferring income and building up as many deductions as possible before the year ends.

However, you might come out ahead of the game by taking the opposite approach if you know you'll be in a higher tax bracket next year, if you've had a below average year this year, or if you are subject to the Alternative Minimum Tax this year. If any of these situations apply to you, you'll probably be better off to defer deductions and move income into this year.

HERE ARE SOME LITTLE-KNOWN YEAR-END TAX STRATEGIES YOU SHOULD CONSIDER

Remove your spouse from the family business payroll. Your spouse's salary is subject to Social Security tax, but if your combined incomes are paid only to you, some of your salary may not be subject to employment taxes. For 2013, earnings above $113,700 are exempt from Social Security tax.

Use credit cards to pay your deductible expenses. Deductible costs placed on your credit card during the year are deductible this year even if payment is not made until next year.

Make a charitable contribution of appreciated securities. You can deduct the full fair market value of the securities. Furthermore, you won't have to pay tax on the increase in their value.

Write off bad debts. You can deduct bad debts as a capital loss, but only in the year in which they become totally

worthless. To substantiate the worthlessness of a bad debt, send a letter demanding payment to the debtor or consider filing a suit against the debtor in small claims court. Be sure to take steps to establish worthlessness before the end of the year.

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taxPOINTS

Late S Corporation election can now be cured by obtaining automatic relief when the election is not made in a timely manner. A late S corporation election can generally be cured if the company had intended to be an S corporation, has consistently reported its income in compliance with S corporation rules, and has not been notified by the IRS that there exists a problem with the election.

Travel and entertainment receipts to be deductible must include the names of the people, the business purpose, where you met, the date, and the cost of the expenses. **Loophole:** No receipt is required by the IRS if per diem allowances are used to substantiate such expenses.

When paying a tax bill indicate specifically what tax you are paying. Include the information on the check you are remitting. **Pitfall:** If you do not indicate for which tax the payment is for the IRS can apply it to any tax liability, which could cause you to incur penalties on a tax you thought was paid.

Added benefits of a Roth IRA. you can continue to make your IRA contributions after age 70 ½ if you have earned income and there is no requirement that you must take distributions at age 70 ½.

How to Get the Best Price When You Sell Your Business

If you're thinking about selling your business, here are some valuable tips that will help you get the best price.

- **Don't base the value of your business on financial statements alone.** Financial statements don't reflect the real value of a business. Sometimes they minimize profits to keep taxes down. In addition, financial statements don't address the future potential of a business, which is really what interests buyers. It's equally important to value your business on realistic growth projections and a buyer's return on investment.
- **Sell at the right time.** When the economy is strong, it's usually a seller's market. When the economy is weak, there are far fewer potential buyers. Don't sell during a recession.
- **Don't be the first to mention price.** Always ask the buyer to make an offer. It might be better than you expected and, no matter what the offer is, you can always negotiate a better deal.
- **Pick the right buyer before you begin to negotiate.** If you offer your business to a competitor or to an employee and the sale falls through, you might regret that you've revealed too much confidential information.
- **Structure the deal to fit your needs.** Ask yourself what you want to do after the sale. If you don't need immediate cash, you'll probably get a better price if a portion of the payment is deferred and you agree to help the buyer learn the business during the ownership transition.

Smarter Purchasing

Buyers will often tell a sales representative that a quoted price is too high because it exceeds the company's budget. While this may cause the rep to lower the price to meet the company's budget, it won't necessarily result in the *best* price because the company's budgeted price might be higher than the seller's lowest price.

For example, assume that the company's budgeted cost is $300. The seller quotes $330. The buyer reveals the company's budget and the rep reduces the quote to $300. The buyer is satisfied because the budget limit has been met, but the company still pays more than it should.

A better negotiating strategy is to tell the sales representative that you'd like to buy, but the price is too high. Ask for a price breakdown and explanation of the components that go into the seller's quote. Have your own pricing information prepared so you can show the rep that his price is too high. If the seller can't explain the quoted price, there's a good chance he'll lower it *below* the company's budget.

Savings Bond Interest Can Be Tax Free When Used For College Tuition

If you have young children, you've probably wondered how you'll be able to pay the high cost of their higher education. If you begin to save now, taxes will make a serious dent in your investment interest. And if you invest in tax free securities, you'll receive substantially lower interest rates.

Thanks to Uncle Sam, a measure of relief is on the way. Interest earned on Series EE savings bonds issued after 1989 can be excluded from your taxable income if the bonds are used to pay for higher education expenses.

WHAT YOU SHOULD KNOW ABOUT SERIES EE BONDS

Series EE bonds are purchased for one-half of their face value. They mature on various dates, depending on current interest rates. For example, a Series EE bond purchased for $500 today is guaranteed to be redeemable for $1,000 twenty years from its date of purchase, while a similar bond purchased in another year could take a different number of years to double in value.

These adjustments in maturity dates make the yield on Series EE bonds competitive with other investments. The bonds can be purchased directly from the U.S. Treasury with no fee or commission charge and are absolutely safe, since they are direct obligations of the federal government. The bonds can be redeemed before their maturity date for less than their face value or can be redeemed later than their maturity date to earn additional interest. Series EE bonds purchases are limited to $20,000 in face value ($10,000 cost) per person per year.

WHO CAN TAKE THE TAX EXCLUSION

The tax exclusion is only available to individuals who purchase Series EE bonds when they are 24 or older. Only the purchaser or the purchaser's spouse can take the exclusion. Bonds that are purchased by your children or bonds that you purchase and transfer to your children do not qualify. Married taxpayers cannot take the exclusion unless they file a joint return.

You can also take the exclusion for yourself if you plan to finance your own education or that of your spouse, but the tax savings is not as great unless you can delay redeeming the bonds for a number of years.

HOW MUCH INTEREST WILL BE TAX FREE

The amount of interest you can exclude from your taxable income depends on the amount of qualified higher education expenses you incur in the year you redeem your savings bonds. If those expenses are greater than the total redemption amount, all of the interest can be excluded subject to certain reductions determined by your income bracket. If the expenses are lower than the redemption amount, the exclusion is reduced by a special formula.

Expenses which qualify for the exclusion are tuition and fees required for enrollment at an institution of higher education such as a university, college, junior college or certain vocational schools. Room and board are not covered and the qualified expenses are reduced by scholarships, grants, or other tuition reduction awards.

Taking advantage of this tax break requires long range planning. Your accountant can give you the professional advice you need for your individual situation.

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If your child works for your business, pay your child a salary. Your child can earn up to $6,100 free of federal income tax. In addition, the child's wages are a deductible business expense. And if your child is under age 18 and your business is not incorporated, the child's wages are not subject to Social Security tax.

Create a qualified retirement plan if you are self-employed or own a business. You have until December 31 to complete the paperwork for a qualified retirement plan that will give you tax deductions for 2013. However, you can fund the plan with tax deductible contributions right up to the date your 2013 tax return is due.

Increase your withholding to compensate for estimated tax underpayment. The IRS considers taxes withheld from your paycheck as payments made evenly throughout the year. Therefore, earlier underpayment of estimated tax can be covered by extra withholdings.

TAX-SAVING STRATEGIES FOR INVESTORS

Use capital losses to offset capital gains. Capital losses are deductible against capital gains on a dollar for dollar basis. In addition, you can deduct capital losses which are in excess of capital gains to offset as much as $3,000 in ordinary income.

Consider buying put options to defer taxes. A put option gives you the right to sell a stock at a pre-determined price (the "exercise price") before a specific date. If you buy puts on a stock you own that has appreciated in value, you can protect your gain and defer taxes on it until next year. Buy puts that you can exercise next year.

Take a loss on a worthless security. You can deduct losses from the worthlessness of a security in the year in which the security becomes worthless. To establish a loss and the date of the loss, sell the security to a friend for a dollar. Some stockbrokers will also purchase the security for a dollar.

REAL ESTATE STRATEGIES TO LOWER TAXES

Determine the best way to report income from an installment sale. If you sold real estate on an installment sale basis in 2013, you can report the total income from the sale this year or you can spread the income over the period of time of the installment agreement. For tax return filing purposes, you can choose either of these methods. Pick the one that's best for you.

Lower your Adjusted Gross Income (AGI). You can partially deduct losses from rental real estate if your AGI is less than $150,000. Lower your AGI by deferring income into 2014 and accelerating deductions into 2013.

Executive Strategies

- **Better decisions:** First, try to find the ideal solution to a problem. Since there is never a perfect solution, you'll always have to seek compromises, but if you first determine what's the absolute best for your company, you'll find that your decisions about compromises will be much easier.
- **Sure road to failure:** Try to please everyone.
- **Mark of leadership:** Accept the fact that tough decisions may be unpopular. And that long periods of time may elapse before your efforts are rewarded.